

**KEARNY COUNTY HOSPITAL**

---

**FINANCIAL STATEMENTS**

**and**

**ADDITIONAL INFORMATION**

**with**

**INDEPENDENT AUDITOR'S REPORT**

---

**YEARS ENDED JUNE 30, 2013 AND 2012**

**George, Bowerman & Noel, P.A.**  
*Certified Public Accountants*

## CONTENTS

|   | <u>Page</u> |
|---|-------------|
| Independent Auditor's Report .....                                  | 1           |
| Management's discussion and analysis .....                          | 3           |
| Financial statements:   |             |
| Balance sheets .....  | 8           |
| Statements of revenues, expenses, and changes in net position ..... | 10          |
| Statements of cash flows .....                                      | 11          |
| Notes to financial statements .....                                 | 13          |
| Additional information:   |             |
| Patient service revenue .....                                       | 24          |
| Operating expenses by functional division .....                     | 25          |

# George, Bowerman & Noel, P.A.

*Certified Public Accountants*

*Business Consultants*

*Tax Advisors*

Epic Center • 301 N. Main, Suite 1350 • Wichita, Kansas 67202 • Telephone (316) 262-6277 • Fax (316) 265-6150

---

## INDEPENDENT AUDITOR'S REPORT

Board of Trustees  
Kearny County Hospital  
Lakin, Kansas

We have audited the accompanying financial statements of Kearny County Hospital, a component unit of Kearny County, Kansas, which comprise the balance sheets as of June 30, 2013 and 2012, and the related statements of revenue, expenses and changes in net position and cash flows for the years then ended, and the related notes to the financial statements.

### Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the provisions of the Kansas Municipal Audit Guide. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of Kearny County Hospital as of June 30, 2013 and 2012, and the changes in financial position and its cash flows for the years then ended in accordance with accounting principles generally accepted in the United States of America.

### Additional Information

Accounting principles generally accepted in the United States of America require that the Management's Discussion and Analysis on pages 3 through 7 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted

in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Our audits were made for the purpose of forming opinions on the basic financial statements taken as a whole. The additional information, as listed in the table of contents, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information is the responsibility of management and was derived from, and relates directly to, the underlying accounting and other records used to prepare the financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the financial statements themselves and other additional procedures, in accordance with auditing standards generally accepted in the United States of America. In our opinion, the additional information is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

*George, Bowennan & Noel, P.A.*

Wichita, Kansas  
January 22, 2014

## KEARNY COUNTY HOSPITAL

### MANAGEMENT'S DISCUSSION AND ANALYSIS

The Kearny County Hospital's (Facility) management's discussion and analysis presents an overview of the Facility's financial activities for the fiscal years ended June 30, 2013 and 2012. Please read it in conjunction with the Facility's financial statements, which begin on page 8.

The Facility has implemented Governmental Accounting Standards Board ("GASB") Statement 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*. Among those guidelines are the components of this section dealing with management's discussion and analysis. Its intent is to provide a brief, objective, and easily readable analysis of the Facility's financial position at June 30, 2013 and 2012 and its financial performance for the years then ended.

#### **Financial Highlights**

- The Facility's net position increased by \$29,409 or .24% in 2013 and decreased by \$1,151,129 or 8.53% in 2012.
- The Facility's net patient service revenue increased by \$1,287,875 or 9.41% in 2013 and by \$829,043 or 6.45% in 2012.
- Contractual allowances, charity care and bad debts reduced gross patient service revenue by \$7,436,894 or 33% of gross patient service revenue in 2013 and by \$5,821,630 or 30% of gross patient service revenue in 2012.
- The Facility reported operating losses in both 2013 (\$1,810,610) and 2012 (\$3,150,053). The operating loss in 2013 decreased by \$1,339,443 or 43% over the loss reported in 2012. The operating loss in 2012 increased by \$801,776 or 34% over 2011.
- Net nonoperating revenues decreased by \$147,682 or 8% in 2013 and increased by \$397,621 or 26% in 2012.

#### **Financial Statements**

The Facility's financial statements are prepared using proprietary fund accounting that focuses on the determination of net position, changes in net position, and cash flows in a manner similar to private-sector businesses. The basic financial statements include a *balance sheet*, *statement of revenue, expenses and changes in net position*, and *statement of cash flows*, followed by notes to the financial statements and schedules of certain additional information. These statements include all restricted and unrestricted assets and all liabilities and deferred inflows and outflows of resources using the accrual basis of accounting. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

The *balance sheet* presents information on the Facility's assets, deferred outflows of resources, liabilities, deferred inflows of resources, with the difference between them reported as net position. Over time, increases or decreases in net position may indicate whether the financial position of the Facility is improving or deteriorating.

The *statement of revenues, expenses and changes in net position* presents both the operating revenues and expenses and nonoperating revenues and expenses along with other changes in net position for the year. This statement is an indication of the success of the Facility's operations over the past year.

The *statement of cash flows* presents the change in cash and cash equivalents for the year resulting from operating activities, noncapital financing activities, capital and related financing activities and investing activities. The primary purpose of this statement is to provide information about the Facility's cash receipts and cash payments during the year.

### **Net Position**

The Facility's net position is the difference between its assets and deferred outflows of resources and its liabilities and deferred inflows of resources as reported in the Balance Sheets on pages 8 and 9. The components of the Facility's net position in each of the past three years are shown in the following table.

|   | June 30,             |                      |                      |
|---|----------------------|----------------------|----------------------|
|   | 2013                 | 2012                 | 2011                 |
| Assets:   |                      |                      |                      |
| Current assets                                      | \$ 4,501,828         | \$ 3,593,905         | \$ 2,904,007         |
| Capital assets, net                                 | 9,929,052            | 11,143,749           | 11,597,234           |
| Other noncurrent assets                             | 2,615                | 31,795               | 75,629               |
| Total assets  | <u>\$ 14,433,495</u> | <u>\$ 14,769,449</u> | <u>\$ 14,576,870</u> |
| Liabilities:  |                      |                      |                      |
| Long-term liabilities                               | \$ —                 | \$ 705,449           | \$ 133,004           |
| Other liabilities                                   | 1,423,440            | 1,722,218            | 950,955              |
| Total liabilities                                   | <u>1,423,440</u>     | <u>2,427,667</u>     | <u>1,083,959</u>     |
| Deferred inflows of resources:                      |                      |                      |                      |
| Deferred revenue – Taxes                            | 638,864              | —                    | —                    |
| Total liabilities and deferred inflows of resources | <u>\$ 2,062,304</u>  | <u>\$ 2,427,667</u>  | <u>\$ 1,083,959</u>  |
| Net position:                                       |                      |                      |                      |
| Invested in capital assets, net                     | \$ 9,929,052         | \$ 10,376,237        | \$ 11,379,110        |
| Restricted  | 543,870              | 603,914              | 534,165              |
| Unrestricted  | 1,898,269            | 1,361,631            | 1,579,636            |
| Total net position                                  | <u>\$ 12,371,191</u> | <u>\$ 12,341,782</u> | <u>\$ 13,492,911</u> |

### **Recent Financial Performance**

The schedule below is a summary of the Facility's revenues, expenses and changes in net position for the past three years.

|                          | Year ended June 30   |                      |                      |
|--------------------------|----------------------|----------------------|----------------------|
|                          | 2013                 | 2012                 | 2011                 |
| Operating revenue        | <u>\$ 15,935,425</u> | <u>\$ 13,715,319</u> | <u>\$ 12,876,757</u> |
| Operating expenses:      |                      |                      |                      |
| Salaries                 | 9,358,934            | 8,901,526            | 7,972,734            |
| Supplies and other       | 7,014,193            | 6,628,653            | 5,930,697            |
| Depreciation             | 1,372,908            | 1,335,193            | 1,321,603            |
| Total operating expenses | <u>17,746,035</u>    | <u>16,865,372</u>    | <u>15,225,034</u>    |
| Operating loss           | <u>(1,810,610)</u>   | <u>(3,150,053)</u>   | <u>(2,348,277)</u>   |

|   | Year ended June 30 (continued) |                |               |
|---|--------------------------------|----------------|---------------|
|   | 2013                           | 2012           | 2011          |
| Nonoperating revenues:  |                                |                |               |
| Taxes   | 1,601,025                      | 1,702,343      | 1,328,984     |
| Investment income   | 9,162                          | 11,591         | 11,794        |
| Interest expense  | (27,758)                       | (22,852)       | (23,086)      |
| Grants and contributions  | 52,083                         | 81,357         | 76,526        |
| Other, net  | 160,190                        | 169,945        | 150,545       |
| Total nonoperating revenues   | 1,794,702                      | 1,942,384      | 1,544,763     |
| Excess of expenses over revenue before capital grants and contributions | (15,908)                       | (1,207,669)    | (803,514)     |
| Capital grants and contributions  | 45,317                         | 56,540         | 20,658        |
| Increase (decrease) in net position                                     | \$ 29,409                      | \$ (1,151,129) | \$ (782,856)  |
| Net position at end of year   | \$ 12,371,191                  | \$ 12,341,782  | \$ 13,492,911 |

### **Operating Losses**

The first component of the overall change in the Facility's net position is its operating income (loss)—generally, the difference between net patient service and the expenses incurred to perform those services. The Facility reported operating losses of \$1,810,610, \$3,150,053 and \$2,348,277 in 2013, 2012 and 2011, respectively.

The primary components of the changes in operating losses are:

- Increases in salary and employee benefit costs for the Facility's employees of \$651,148 or 6% in 2013 and \$1,393,545 or 14% in 2012.
- Increases in supplies and other expenses of \$191,807 or 5% in 2013 and \$233,203 or 6% in 2012.
- Contractual allowances, charity care and bad debt expense increased by \$1,615,264 in 2013 and by \$696,438 in 2012.
- Net operating revenue increased \$2,220,106 or 16% in 2013 and \$838,562 or 7% in 2012. The significant change in 2013 was due, in part, to the Facility qualifying for incentive payments of \$932,270 from the Medicare and Medicaid programs upon meeting the requirements for a qualified electronic health record (EHR) system in 2013.

The rate of healthcare inflation has a direct effect on the cost of services provided by the Facility. A component of the Facility's costs are expenses for medical supplies and prescription drugs. Some of the major factors contributing to the increased medical supply and drug costs include the introduction of new drugs that cannot be obtained in generic form, and changes in therapeutic mix.

### **Nonoperating Revenues and Expenses**

Nonoperating revenues consist primarily of property taxes levied by the County, investment earnings, and grants and contributions.

### **The Facility's Cash Flows**

Changes in the Facility's cash flows are consistent with changes in operating losses and nonoperating revenues and expenses, discussed earlier.

### **Capital Assets**

The Facility had \$9,929,052, \$10,376,237 and \$11,379,110 invested in capital assets, net of accumulated depreciation and related debt, at June 30, 2013, 2012 and 2011, respectively, as detailed in Note 6 to the financial statements. The Facility had expenditures of approximately \$158,000 and \$882,000 for equipment in 2013 and 2012, respectively.

### **Long-term Debt**

At June 30, 2012, the Facility had a promissory note payable outstanding of \$767,512 for an electronic health record system, as detailed in Note 7 to the financial statements. The note was paid off during the year ended June 30, 2013.

### **Other Economic Factors**

Management expects the current economic conditions to continue over the next year.

### **Issues Facing the Facility**

There are issues facing the Facility that could result in material changes in its financial position in the long term. Among these issues are:

- Risks related to Medicare and Medicaid reimbursement. A significant portion of the Facility's revenues are derived from the Medicare program, which provides certain healthcare benefits to beneficiaries who are over 65 years of age or disabled, and the Medicaid program, funded jointly by the federal government and the states, which provides medical assistance to certain needy individuals and families. The funding of these programs by the federal and state governments face increasing pressure due to the significant increases in the costs of providing healthcare services in recent years.
- Employment and labor issues. The Facility is a major employer within the community, employing a complex mix of professional, technical, clerical, maintenance, dietary, and other workers. Risks include personal tort actions, work-related injuries and exposure to hazardous materials. A relative shortage of nursing and other medical professional/technical employees within the state, is an issue that is causing salary and benefits costs to increase at significant rates.
- Technology and services. Scientific and technological advances, new procedures, drugs and appliances, preventive medicine, and outpatient healthcare delivery may reduce utilization and revenues for the Facility in the future. Technological advances continue to accelerate the need to acquire sophisticated and expensive equipment and services for diagnosis and treatment of illnesses and diseases.
- Increasing numbers of uninsured and underinsured patients. Due to the significant increases and high cost of healthcare insurance premiums in recent years, increasing numbers of patients of the Facility are finding it more and more difficult to obtain or maintain adequate health insurance coverage. This trend could increase the levels of uncompensated care provided by the Facility.



### **Contacting The Facility's Financial Management**

This financial report is designed to provide our patients, suppliers, taxpayers, and creditors with a general overview of the Facility's finances and to show the Facility's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Facility's Administration Department, at Kearny County Hospital, 500 N. Thorpe St., Lakin, Kansas 67860.

**KEARNY COUNTY HOSPITAL**

**BALANCE SHEETS**

**ASSETS**

|   | <u>June 30,</u>      |                      |
|---|----------------------|----------------------|
|   | <u>2013</u>          | <u>2012</u>          |
| Current assets:   |                      |                      |
| Cash (Notes 1 and 3)  | \$ 808,635           | \$ 10,763            |
| Assets whose use is limited (Notes 1 and 3)   | 1,156,257            | 779,985              |
| Accounts receivable, net of allowance for doubtful accounts of<br>\$808,558 in 2013 and \$666,679 in 2012 (Notes 1 and 4) | 1,869,488            | 1,608,198            |
| Current portion of employee receivables   | 29,180               | 43,833               |
| Due from third-party insurance programs (Note 2)  | —                    | 701,676              |
| Inventories (Note 1)  | 304,643              | 270,317              |
| Prepaid expenses and other  | <u>333,625</u>       | <u>179,133</u>       |
| Total current assets  | <u>4,501,828</u>     | <u>3,593,905</u>     |
| <br>Long-term portion of employee receivables   | <br><u>2,615</u>     | <br><u>31,795</u>    |
| <br>Property and equipment, at cost (Notes 1 and 6):  |                      |                      |
| Land  | 97,298               | 97,298               |
| Land improvements   | 634,019              | 634,019              |
| Buildings and fixed equipment   | 18,092,742           | 18,061,745           |
| Movable equipment   | 4,818,109            | 4,110,798            |
| Projects in progress  | <u>31,279</u>        | <u>611,376</u>       |
|   | 23,673,447           | 23,515,236           |
| Less accumulated depreciation   | <u>13,744,395</u>    | <u>12,371,487</u>    |
| Property and equipment, net of accumulated depreciation   | <u>9,929,052</u>     | <u>11,143,749</u>    |
| Total assets  | <u>\$ 14,433,495</u> | <u>\$ 14,769,449</u> |

The accompanying notes are an integral  
part of the financial statements.

# **LIABILITIES, DEFERRED INFLOWS OF RESOURCES AND NET POSITION**

|   | <u>June 30,</u>      |                      |
|---|----------------------|----------------------|
|   | <u>2013</u>          | <u>2012</u>          |
| Current liabilities:  |                      |                      |
| Accounts payable  | \$ 366,081           | \$ 414,178           |
| Salaries payable  | 385,529              | 355,123              |
| Compensated absences payable (Note 1)                             | 260,944              | 277,605              |
| Payroll taxes payable   | 5,215                | 18,500               |
| Due to third-party insurance programs (Note 2)                    | 57,655               | —                    |
| Accrued interest payable  | —                    | 5,304                |
| Other accrued expenses  | 348,016              | 93,835               |
| Current portion of long-term debt (Note 7)                        | —                    | 62,063               |
| Note payable to bank (Note 8)                                     | <u>—</u>             | <u>495,610</u>       |
| Total current liabilities   | <u>1,423,440</u>     | <u>1,722,218</u>     |
| Long-term debt (Note 7)   | <u>—</u>             | <u>705,449</u>       |
| Total liabilities   | <u>1,423,440</u>     | <u>2,427,667</u>     |
| Deferred inflows of resources:                                    |                      |                      |
| Deferred revenue – Taxes  | <u>638,864</u>       | <u>—</u>             |
| Net position (Notes 1 and 3):                                     |                      |                      |
| Invested in capital assets, net of related debt                   | 9,929,052            | 10,376,237           |
| Restricted:   |                      |                      |
| Expendable for capital asset acquisition                          | 543,870              | 603,914              |
| Unrestricted  | <u>1,898,269</u>     | <u>1,361,631</u>     |
| Total net position  | <u>12,371,191</u>    | <u>12,341,782</u>    |
| Total liabilities, deferred inflows of resources and net position | <u>\$ 14,433,495</u> | <u>\$ 14,769,449</u> |

**KEARNY COUNTY HOSPITAL**  
**STATEMENTS OF REVENUES, EXPENSES, AND CHANGES**  
**IN NET POSITION**

|  | <u>Year ended June 30,</u> |                      |
|--|----------------------------|----------------------|
|  | <u>2013</u>                | <u>2012</u>          |
| Operating revenues:  |                            |                      |
| Net patient service revenue (Note 1)                                     | \$ 14,970,959              | \$ 13,683,084        |
| Other  | <u>964,466</u>             | <u>32,235</u>        |
| Total operating revenue  | <u>15,935,425</u>          | <u>13,715,319</u>    |
| Operating expenses:  |                            |                      |
| Salaries   | 9,358,934                  | 8,901,526            |
| Supplies and other   | 7,014,193                  | 6,628,653            |
| Depreciation (Note 1)  | <u>1,372,908</u>           | <u>1,335,193</u>     |
| Total operating expenses   | <u>17,746,035</u>          | <u>16,865,372</u>    |
| Operating loss   | <u>(1,810,610)</u>         | <u>(3,150,053)</u>   |
| Nonoperating revenues:   |                            |                      |
| Tax revenues   | 1,601,025                  | 1,702,343            |
| Investment income  | 9,162                      | 11,591               |
| Interest expense   | (27,758)                   | (22,852)             |
| Noncapital grants and contributions                                      | 44,482                     | 57,397               |
| Transfers from Kearny County for operations                              | 7,601                      | 23,960               |
| Other  | <u>160,190</u>             | <u>169,945</u>       |
| Total nonoperating revenues  | <u>1,794,702</u>           | <u>1,942,384</u>     |
| Excess of expenses over revenues before contributions for capital assets | (15,908)                   | (1,207,669)          |
| Transfers from Kearny County for capital assets                          | <u>45,317</u>              | <u>56,540</u>        |
| Increase (decrease) in net position                                      | 29,409                     | (1,151,129)          |
| Net position at beginning of year  | <u>12,341,782</u>          | <u>13,492,911</u>    |
| Net position at end of year  | <u>\$ 12,371,191</u>       | <u>\$ 12,341,782</u> |

The accompanying notes are an integral  
part of the financial statements.

**KEARNY COUNTY HOSPITAL**  
**STATEMENTS OF CASH FLOWS**

|  | <u>Year ended June 30,</u> |                    |
|--|----------------------------|--------------------|
|  | <u>2013</u>                | <u>2012</u>        |
| Cash flows from operating activities:                                      |                            |                    |
| Receipts from and on behalf of patients                                    | \$ 15,469,000              | \$ 13,144,785      |
| Payments to suppliers and contractors                                      | (7,010,212)                | (6,503,482)        |
| Payments to employees  | (9,345,189)                | (8,793,290)        |
| Other receipts and payments, net   | <u>964,466</u>             | <u>32,235</u>      |
| Net cash flows provided (used) by operating activities                     | <u>78,065</u>              | <u>(2,119,752)</u> |
| Cash flows from noncapital financing activities:                           |                            |                    |
| Property taxes for operations  | 2,239,889                  | 1,702,343          |
| Grants and contributions   | 44,482                     | 57,397             |
| Transfers from Kearny County for operations                                | 7,601                      | 23,960             |
| Other  | <u>160,190</u>             | <u>169,945</u>     |
| Net cash flows provided by noncapital financing activities                 | <u>2,452,162</u>           | <u>1,953,645</u>   |
| Cash flows from capital and related financing activities:                  |                            |                    |
| Purchases of property and equipment  | (158,211)                  | (443,791)          |
| Payments on long-term debt   | (800,574)                  | (94,962)           |
| Proceeds from note payable to bank   | 4,579,451                  | 5,797,885          |
| Payments on note payable to bank   | (5,075,061)                | (5,131,819)        |
| Transfers from Kearny County for capital assets                            | <u>45,317</u>              | <u>56,540</u>      |
| Net cash flows provided (used) by capital and related financing activities | <u>(1,409,078)</u>         | <u>183,853</u>     |
| Cash flows from investing activities:                                      |                            |                    |
| Net change in employee receivables   | 43,833                     | 49,744             |
| Investment income  | <u>9,162</u>               | <u>11,591</u>      |
| Net cash flows provided by investing activities                            | <u>52,995</u>              | <u>61,335</u>      |
| Increase in cash and cash equivalents                                      | 1,174,144                  | 79,081             |
| Cash and cash equivalents at beginning of year                             | <u>790,748</u>             | <u>711,667</u>     |
| Cash and cash equivalents at end of year                                   | <u>\$ 1,964,892</u>        | <u>\$ 790,748</u>  |

The accompanying notes are an integral  
part of the financial statements.

**KEARNY COUNTY HOSPITAL**  
**STATEMENTS OF CASH FLOWS - continued**

|  | <u>Year ended June 30,</u> |                       |
|--|----------------------------|-----------------------|
|  | <u>2013</u>                | <u>2012</u>           |
| Reconciliation of cash and cash equivalents to balance sheets:                                     |                            |                       |
| Cash and cash equivalents in current assets:   |                            |                       |
| Cash   | \$ 808,635                 | \$ 10,763             |
| Assets whose use is limited  | <u>1,156,257</u>           | <u>779,985</u>        |
| Total cash and cash equivalents  | <u>\$ 1,964,892</u>        | <u>\$ 790,748</u>     |
| Reconciliation of operating loss to net cash provided (used) by operating activities:              |                            |                       |
| Operating loss   | \$ (1,810,610)             | \$ (3,150,053)        |
| Adjustments to reconcile operating loss to net cash flows provided (used) by operating activities: |                            |                       |
| Depreciation   | 1,372,908                  | 1,335,193             |
| Provision for doubtful accounts  | 819,202                    | 725,144               |
| Net (increases) decreases in current assets:   |                            |                       |
| Accounts receivable  | (1,080,492)                | (777,875)             |
| Inventories  | (34,326)                   | (25,976)              |
| Due from third-party insurance programs  | 701,676                    | (485,568)             |
| Other  | (154,492)                  | (52,452)              |
| Net increases (decreases) in current liabilities:  |                            |                       |
| Accounts payable   | (48,097)                   | 170,906               |
| Salaries and wages payable   | 30,406                     | 87,112                |
| Compensated absences payable   | (16,661)                   | 21,124                |
| Payroll taxes payable  | (13,285)                   | 3,301                 |
| Due to third-party insurance programs  | 57,655                     | -                     |
| Other accrued expenses   | <u>254,181</u>             | <u>29,392</u>         |
| Net cash provided (used) by operating activities   | <u>\$ 78,065</u>           | <u>\$ (2,119,752)</u> |

**KEARNY COUNTY HOSPITAL**  
**NOTES TO FINANCIAL STATEMENTS**

**June 30, 2013 and 2012**

**1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

This summary of significant accounting policies is presented to assist in understanding the Facility's financial statements. The financial statements and notes are representations of the Facility's management, which is responsible for their integrity and objectivity. These accounting policies conform to generally accepted accounting principles and have been consistently applied in the preparation of the financial statements.

**Organization and business activity**

Kearny County Hospital (Facility) is owned by Kearny County, Kansas and is governed by a Board of Trustees. The Facility provides acute, skilled, intermediate, assisted living, self-care, clinic and home health services. The Board of County Commissioners appoints the members of the Board of Trustees. For this reason, the Facility is considered to be a component unit of Kearny County, Kansas.

**Proprietary fund accounting**

The Facility's financial statements are comprised solely of an enterprise fund that uses proprietary accounting. Revenues and expenses are recognized on the accrual basis using the economic resources measurement focus.

The Facility prepares its financial statements as a business-type activity in conformity with applicable pronouncements of the Governmental Accounting Standards Board (GASB). Pursuant to GASB Statement No. 20, *Accounting and Financial Reporting for Proprietary Funds and Other Governmental Entities That Use Proprietary Fund Accounting*, as amended, the Facility has elected to apply the provisions of all relevant pronouncements of the Financial Accounting Standards Board (FASB), including those issued after November 30, 1989, that do not conflict with or contradict GASB pronouncements.

**Use of estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

**Operating revenues and expenses**

The Facility's statement of revenues, expenses, and changes in net position distinguishes between operating and non-operating revenues and expenses. Operating revenues result from exchange transactions associated with providing health care services – the Facility's principal activity. Non-exchange revenues, including taxes, grants, and contributions received for purposes other than capital asset acquisitions, are reported as non-operating revenues. Operating expenses are all expenses incurred to provide health care services, other than financing costs.

**Cash and cash equivalents**

For purposes of the statement of cash flows, the Facility considers all highly liquid debt instruments with an original maturity of three months or less to be cash and cash equivalents.

## 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### Patient accounts receivable

The Facility reports patient accounts receivable for services rendered at net realizable amounts from third-party payers, patients and others. The Facility provides an allowance for uncollectible accounts based upon a review of outstanding receivables, historical collection information, payer mix trends, and existing economic conditions. As a service to patients, the Facility bills third-party payers directly and bills the patient when the patient's liability is determined. Patient accounts receivable are generally due in full when billed. If the patient is unable to pay the full amount at the time the patient is billed, the Facility negotiates a payment plan whereby monthly payments are made by the patient on the account. Accounts are considered delinquent and subsequently written off as bad debts based on individual credit evaluation and specific circumstances of the account. If future actual default rates on accounts receivable differ from those currently anticipated, the Facility may have to adjust its allowance for doubtful accounts, which would affect earnings in the period the adjustments are made.

### Inventories

Inventories are stated at cost as determined by the first-in, first-out method.

### Capital assets

The Facility's capital assets that are \$5,000 or greater, are recorded at cost at the date of acquisition, or fair value at the date of donation if acquired by gift. All capital assets other than land are depreciated or amortized (in the case of capital leases) using the straight-line method of depreciation using the following estimated useful lives:

|                         | <u>Estimated<br/>useful lives</u> |
|-------------------------|-----------------------------------|
| Land improvements ..... | 10 - 20 years                     |
| Buildings .....         | 5 - 40 years                      |
| Fixed equipment .....   | 5 - 20 years                      |
| Movable equipment ..... | 5 - 20 years                      |

The costs of maintenance and repairs are charged to operating expenses as incurred. The costs of significant additions, renewals and betterments to depreciable properties are capitalized and depreciated over the remaining or extended estimated useful lives of the item or the properties. When depreciable property is retired or otherwise disposed of, the related costs and accumulated depreciation are removed from the accounts and any gain or loss is reflected as non-operating revenue (expense).

### Net patient service revenue

The Facility has agreements with third-party payors that provide for payments to the Facility at amounts different from its established rates. Payment arrangements include prospectively determined rates per discharge, reimbursed costs, per diem payments, and discounted charges. Net patient service revenue is reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. Retroactive adjustments are accrued on an estimated basis in the period the related services are rendered and adjusted in future periods as final settlements are determined.



## **1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

### **Charity care**

The Facility provides care without charge or at amounts less than its established rates to patients meeting certain criteria under its charity care policy based on current poverty level guidelines. Because the Facility does not pursue collection of amounts determined to qualify as charity care, these amounts are not reported as net patient service revenue. Charges excluded from revenue under the Facility's charity care policy were \$127,462 and \$116,077 for June 30, 2013 and 2012, respectively.

### **Compensated absences**

Employees of the Facility are entitled to paid time off depending on length of service and whether they are full or part time. Upon resignation, termination or retirement from service with the Facility, employees are entitled to payment for all accrued paid time off, up to the allowable maximum. The Facility accrues the paid time off benefits as earned.

### **Grants and contributions**

From time to time, the Facility receives grants and contributions from government agencies, private organizations, and individuals. Revenues from grants and contributions are recognized when all eligibility requirements, including time requirements are met. Grants and contributions may be restricted for either specific operating purposes or for capital purposes. Amounts that are unrestricted or that are restricted to a specific operating purpose are reported as non-operating revenue. Amounts restricted to capital acquisitions are reported after non-operating revenues and expenses. When the Facility has both restricted and unrestricted resources available to finance a particular program, it is the Facility's policy to use restricted resources before unrestricted resources.

### **Net position**

Net position of the Facility is classified into three components. *Invested in capital assets, net of related debt* consist of capital assets net of accumulated depreciation and reduced by the current balances of any outstanding borrowings used to finance the purchase or construction of those assets. *Restricted expendable net position* consists of assets, less related liabilities, that must be used for a particular purpose, as specified by creditors, grantors, or contributors external to the Facility, including amounts deposited with trustees as required by indentures, reduced by the outstanding balances of any related borrowings. *Unrestricted net position* are remaining assets less remaining liabilities and deferred inflows that do not meet the definition of *invested in capital assets, net of related debt* or *restricted*.

### **Risk management**

The Facility is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; injuries to employees; natural disasters; and employee health benefits. Commercial insurance coverage is purchased for claims arising from such matters. Settled claims have not exceeded this commercial insurance coverage in any of the three preceding years.

The Facility pays fixed premiums for annual medical malpractice coverage under an occurrence-basis policy. The Facility accrues the expenses of its share of malpractice claim costs, if any, of reported and unreported incidents of potential improper professional service occurring during the year by estimating the probable ultimate cost of any incident. Based on the Facility's own claims experience, no accrual, for medical malpractice costs has been made in the accompanying financial statements. It is possible that this estimate could change materially in the near term.

The Facility has implemented a partially self-funded insurance plan to administer its employee health insurance benefits. Liabilities under this plan are estimated based on settled claims, frequency of claims and other economic factors. Claims incurred, but not reported, are recorded as a portion of the estimated liability.

## **1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)**

### **Change in accounting principle**

Effective, July 1, 2012, the Facility implemented the provisions of GASB Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources and Net Position* and GASB Statement No. 65, *Items Previously Reported As Assets and Liabilities*. GASB Statement No. 63 provides guidance for reporting deferred inflows and deferred outflows of resources and GASB Statement No. 65 provides additional guidance on reclassifying, as deferred inflows of resources and deferred outflows of resources, certain items that were previously reported as assets and liabilities. The implementation of the applicable requirements of these GASB statements was accomplished by a retroactive adjustment to the net position balance at July 1, 2011. Additionally, the term "net assets" was replaced with the term "net position".

A deferred inflow of resources is defined as an acquisition of net position applicable to a future reporting period. Taxes of \$638,834 received from Kearny County in 2013 to fund 2014 operations are identified on the Facility's balance sheet as a deferred inflow. A deferred outflow of resources is the consumption of net position that is applicable to a future reporting period. There were no items identified by the Facility that met the definition of a deferred outflow of resources.

### **Reclassifications**

Certain reclassifications have been made to the 2012 financial statements to conform to the 2013 presentation. These other reclassifications had no effect on the change in net position.

### **Subsequent events**

Subsequent events have been evaluated through January 22, 2014, which is the date the financial statements were available to be issued.

## **2. ESTIMATED THIRD-PARTY PAYOR SETTLEMENTS**

The Facility has agreements with third-party payers that provide for payments to the Facility at amounts different from its established rates. These payment arrangements include:

- **Medicare** – Inpatient and outpatient services are paid based on cost reimbursement methodologies. The Facility is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual cost reports by the Facility and reviews thereof by the Medicare fiscal intermediary. The Facility's classification of patients under the Medicare program and appropriateness of their admission are subject to an independent review by a peer review organization under contract with the Facility. The Facility's Medicare cost reports have been reviewed by the Medicare fiscal intermediary through June 30, 2010.
- **Medicaid** – For the year ended June 30, 2012 and for the period from July 1, to December 31, 2012, inpatient and outpatient services rendered to program beneficiaries are reimbursed under a cost reimbursement methodology for patients who are not part of a Medicaid managed care network. The Facility is reimbursed for cost reimbursable items at tentative rates with final settlement determined after submission of annual cost reports by the Facility and reviews thereof by the Medicaid fiscal intermediary. As of January 1, 2013, the Facility is reimbursed under the State of Kansas KanCare program utilizing the Medicaid fee schedule plus a cost adjustment factor.

Inpatient long-term care services for the years ended June 30, 2013 and 2012 are paid at prospectively determined per diem rates that are based on the patient's acuity.

## 2. ESTIMATED THIRD-PARTY PAYOR SETTLEMENTS(continued)

Approximately 26% and 28% of net patient service revenue is from participation in the Medicare program for the years ended June 30, 2013 and 2012, respectively. Laws and regulations governing the Medicare program are complex and subject to interpretation and change. As a result, it is reasonably possible that recorded estimates will change materially in the near term.

Pursuant to enactment of the *American Recovery and Reinvestment Act of 2009*, the Medicare and Medicaid programs implemented programs to provide for one-time incentive payments for eligible hospitals that demonstrate meaningful use of certified electronic health records systems (EHR).

Under Medicare's incentive program, hospitals are generally eligible to receive these incentive payments for up to four years for reasonable costs incurred for certified EHR systems multiplied by the hospital's Medicare utilization plus 20%, up to 100% of the reasonable costs incurred. Payments under the Medicaid program are generally available for up to four years based upon a formula determined by the state and approved by the Centers for Medicare and Medicaid Services (CMS). Final amounts for any payment year are contingent upon the hospital continuing to meet increasing meaningful use criteria and, accordingly, are subject to review and approval by the Medicare and Medicaid programs fiscal intermediaries. As a result, it is reasonably possible that final determined amounts may differ materially from initial revenues recorded under these programs.

During 2013, the Facility met the initial requirements to receive EHR incentive payments from the Medicare program and accordingly, \$932,270 of other operating revenue has been recorded for the year ended June 30, 2013.

The Facility has also entered into payment agreements with certain commercial insurance carriers and other third-party payor programs. The basis for payment to the Facility under these agreements includes prospectively determined rates per discharge, discounts from established charges and cost reimbursement.

## 3. CASH AND ASSETS WHOSE USE IS LIMITED

Cash and assets whose use is limited consisted of the following:

|  | June 30,            |                   |
|--|---------------------|-------------------|
|  | 2013                | 2012              |
| Unrestricted demand and time deposit accounts  | \$ 808,635          | \$ 10,763         |
| Assets whose use is limited:                   |                     |                   |
| By Board of Trustees:                          |                     |                   |
| Savings accounts – capital assets acquisitions | 434,039             | 176,071           |
| Savings accounts – health insurance reserve    | 178,348             | —                 |
| By others:                                     |                     |                   |
| Expendable for capital asset acquisitions      | 543,870             | 603,914           |
| Totals   | <u>\$ 1,964,892</u> | <u>\$ 790,748</u> |

Assets whose use is limited by the Board of Trustees are to be used for the replacement of capital assets, for the purchase of additional capital assets and self-fund health insurance claims. These assets may be utilized for other purposes at the discretion of the Board.

### 3. CASH AND ASSETS WHOSE USE IS LIMITED (continued)

The amounts expendable for capital asset acquisitions relate to distributions made to the Facility from a charitable trust. The Facility, along with other trust beneficiaries, received annual distributions of trust net income until 2010 at which time, the trust was terminated and all undistributed net income along with trust principal were distributed to the trust beneficiaries. Distributions to the Facility are to be used for the replacement of capital assets or for the purchase of additional capital assets. Distributions may be used for other purposes upon unanimous vote of the Board of Trustees and approval by the trustee bank.

#### Deposits

Custodial credit risk for deposits is the risk that in the event of bank failure, the Facility's deposits may not be returned or the Facility will not be able to recover collateral securities in the possession of an outside party. The Facility's policy follows applicable State statutes and requires deposits to be 100% secured by collateral (pledged securities) valued at market, less the amount of the Federal Deposit Insurance Corporation (FDIC) insurance. State statutes define the allowable pledged securities.

At year end, the carrying amount of the Facility's deposits was \$1,962,908 with the bank balances of such accounts being \$2,039,568. Of the bank balances, \$262,437 was secured by federal depository insurance and the remaining balance of \$1,777,131 was covered by collateral held by the Facility's custodial bank in joint custody in the name of the Facility and its bank. The fair value of those pledged securities held by the Facility's custodial bank was \$2,211,648 at June 30, 2013.

#### Investment policies

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligation. The Facility's investing activities are managed under the custody of senior management. Investing is performed in accordance with investment policies adopted by the Board of Trustees and in compliance with State statutes.

Applicable state statutes authorize the Facility to invest in (1) temporary notes or no-fund warrants issued by the Facility (2) time deposit, open accounts or certificates of deposit, with maturities of not more than two years, in commercial banks; (3) time certificates of deposit, with maturities of not more than two years, with state or federally chartered savings and loan associations or federally chartered savings banks, (4) repurchase agreements with commercial banks, state or federally chartered savings and loan associations or federally chartered savings banks; (5) United States treasury bills or notes with maturities as the governing body shall determine, but not exceeding two years; (6) the municipal investment pool maintained by the State Treasurer's office, and (7) trust departments of commercial banks.

### 4. CONCENTRATIONS OF CREDIT RISK

The Facility grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of gross accounts receivable from patients and third-party payors at June 30, 2013 and 2012 was as follows:

|             | June 30,    |             |
|-------------|-------------|-------------|
|             | 2013        | 2012        |
| Medicare    | 25%         | 26%         |
| Medicaid    | 17          | 10          |
| Blue Cross  | 13          | 11          |
| Commercial  | 11          | 13          |
| Private pay | 34          | 40          |
|             | <u>100%</u> | <u>100%</u> |

## 5. PENSION PLAN

The Facility maintains a contributory pension plan for all employees in lieu of social security. Prior to July 1, 1997, employees made contributions equal to 5% of their gross compensation. The Facility contribution was 10% of the employees' gross compensation for those employed for two years or more and 5% for all others. Effective July 1, 1997, employees are required to contribute the same percentage required under the Social Security laws (OASDI). The Facility is required to make a matching contribution in the same amount. An additional 3% contribution is made by the Facility on behalf of all employees continuously employed for three years or more. Voluntary employee contributions may be made up to a specified percent of eligible compensation not to exceed \$17,500 and \$17,000 for 2013 and 2012, respectively. Benefits are funded by an annuity contract with an insurance company. The total cost of the plan was \$749,847 and \$715,023 for 2013 and 2012, respectively. Employee and employer contributions vest immediately.

## 6. CAPITAL ASSETS

Capital asset additions, disposals, and balances for the years ended June 30, 2013 were as follows:

|   | Balance At<br>June 30,<br>2012 | Additions      | Disposals | Transfers | Balance At<br>June 30,<br>2013 |
|---|--------------------------------|----------------|-----------|-----------|--------------------------------|
| Capital assets not being depreciated:       |                                |                |           |           |                                |
| Land  | \$ 97,298                      | \$ —           | \$ —      | \$ —      | \$ 97,298                      |
| Projects in progress                        | 611,376                        | 64,161         | —         | (644,258) | 31,279                         |
| Total capital assets not being depreciated  | 708,674                        | 64,161         | —         | (644,258) | 128,577                        |
| Capital assets being depreciated:           |                                |                |           |           |                                |
| Land improvements                           | 634,019                        | —              | —         | —         | 634,019                        |
| Buildings and fixed equipment               | 18,061,745                     | 30,997         | —         | —         | 18,092,742                     |
| Movable equipment                           | 4,110,798                      | 63,053         | —         | 644,258   | 4,818,109                      |
| Total capital assets being depreciated      | 22,806,562                     | 94,050         | —         | 644,258   | 23,544,870                     |
| Less accumulated depreciation for:          |                                |                |           |           |                                |
| Land improvements                           | 310,733                        | 39,958         | —         | —         | 350,691                        |
| Buildings and fixed equipment               | 8,988,782                      | 849,842        | —         | —         | 9,838,624                      |
| Movable equipment                           | 3,071,972                      | 483,108        | —         | —         | 3,555,080                      |
| Total accumulated depreciation              | 12,371,487                     | 1,372,908      | —         | —         | 13,744,395                     |
| Total capital assets being depreciated, net | 10,435,075                     | (1,278,858)    | —         | 644,258   | 9,800,475                      |
| Total capital assets, net                   | \$ 11,143,749                  | \$ (1,214,697) | \$ —      | \$ —      | \$ 9,929,052                   |

## 6. CAPITAL ASSETS (continued)

Capital asset additions, disposals, and balances for the years ended June 30, 2012 were as follows:

|   | Balance At<br>June 30,<br>2011 | Additions           | Disposals     | Transfers   | Balance At<br>June 30,<br>2012 |
|---|--------------------------------|---------------------|---------------|-------------|--------------------------------|
| Capital assets not being depreciated:       |                                |                     |               |             |                                |
| Land  | \$ 97,298                      | \$ —                | \$ —          | \$ —        | \$ 97,298                      |
| Projects in progress                        | <u>199,263</u>                 | <u>412,113</u>      | <u>—</u>      | <u>—</u>    | <u>611,376</u>                 |
| Total capital assets not being depreciated  | <u>296,561</u>                 | <u>412,113</u>      | <u>—</u>      | <u>—</u>    | <u>708,674</u>                 |
| Capital assets being depreciated:           |                                |                     |               |             |                                |
| Land improvements                           | 634,019                        | —                   | —             | —           | 634,019                        |
| Buildings and fixed equipment               | 18,005,205                     | 56,540              | —             | —           | 18,061,745                     |
| Movable equipment                           | <u>3,751,261</u>               | <u>413,055</u>      | <u>53,518</u> | <u>—</u>    | <u>4,110,798</u>               |
| Total capital assets being depreciated      | <u>22,390,485</u>              | <u>469,595</u>      | <u>53,518</u> | <u>—</u>    | <u>22,806,562</u>              |
| Less accumulated depreciation for:          |                                |                     |               |             |                                |
| Land improvements                           | 270,739                        | 39,994              | —             | —           | 310,733                        |
| Buildings and fixed equipment               | 8,068,537                      | 920,245             | —             | —           | 8,988,782                      |
| Movable equipment                           | <u>2,750,536</u>               | <u>374,954</u>      | <u>53,518</u> | <u>—</u>    | <u>3,071,972</u>               |
| Total accumulated depreciation              | <u>11,089,812</u>              | <u>1,335,193</u>    | <u>53,518</u> | <u>—</u>    | <u>12,371,487</u>              |
| Total capital assets being depreciated, net | <u>11,300,673</u>              | <u>(865,598)</u>    | <u>—</u>      | <u>—</u>    | <u>10,435,075</u>              |
| Total capital assets, net                   | <u>\$ 11,597,234</u>           | <u>\$ (453,485)</u> | <u>\$ —</u>   | <u>\$ —</u> | <u>\$ 11,143,749</u>           |

## 7. LONG-TERM DEBT

The following is a summary of changes in long-term debt for the year ended June 30, 2013 and 2012:

|                           | Balance At<br>June 30,<br>2012 | Additions        | Reductions        | Balance At<br>June 30,<br>2013 | Amounts<br>Due Within<br>One Year |
|---------------------------|--------------------------------|------------------|-------------------|--------------------------------|-----------------------------------|
| Capital lease obligations | \$ -                           | \$ -             | \$ -              | \$ -                           | \$ -                              |
| Note Payable              | <u>767,512</u>                 | <u>15,592</u>    | <u>783,104</u>    | <u>-</u>                       | <u>-</u>                          |
| Total                     | <u>\$ 767,512</u>              | <u>\$ 15,592</u> | <u>\$ 783,104</u> | <u>\$ -</u>                    | <u>\$ -</u>                       |

|                           | Balance At<br>June 30,<br>2011 | Additions         | Reductions       | Balance At<br>June 30,<br>2012 | Amounts<br>Due Within<br>One Year |
|---------------------------|--------------------------------|-------------------|------------------|--------------------------------|-----------------------------------|
| Capital lease obligations | \$ 28,623                      | \$ -              | \$ 28,623        | \$ -                           | \$ -                              |
| Note Payable              | <u>189,501</u>                 | <u>637,575</u>    | <u>59,564</u>    | <u>767,512</u>                 | <u>62,063</u>                     |
| Total                     | <u>\$ 218,124</u>              | <u>\$ 637,575</u> | <u>\$ 88,187</u> | <u>\$ 767,512</u>              | <u>\$ 62,063</u>                  |

### Capitalized lease obligations

The Facility has entered into capital lease agreements for the acquisition of certain capital assets, including a new lease for the acquisition and installation of an electronic health record (EHR) system in 2011. The lease for the EHR system with a principal balance of approximately \$400,000 was converted to a note payable during 2012. Interest incurred under the leases was \$6,808 for the year ended June 30, 2012.

### Note Payable

During 2012, the Facility entered into a note payable for the principal amount of \$800,000 for the acquisition and installation of an electronic health record (EHR) system. The EHR project was completed in 2013 and the note was fully retired with proceeds from the Medicare and Medicaid EHR incentive programs received during 2013. Interest expense incurred on the note for the years ended June 30, 2013 and 2012 was \$15,246 and \$9,897, respectively.

## 8. NOTE PAYABLE TO BANK

The Facility has a revolving line of credit agreement with a local bank. The maximum principal that can be borrowed is \$800,000 and carries a fixed interest rate of 3.0%. Interest expense incurred on the obligation for the years ended June 30, 2013 and 2012 was \$9,905 and \$6,147, respectively. The note is collateralized by accounts receivable and it is management's intention to pursue the renewal of the agreement when it expires in March of 2014.

## **9. OTHER POST EMPLOYMENT BENEFITS**

As provided by K.S.A. 12-5040, the Facility is required to allow qualifying retirees to participate in the group health insurance plan. While each retiree is required to pay the full amount of the applicable premium, conceptually, the Facility is subsidizing the retirees because each participant is charged a level premium regardless of age. However, the cost of the subsidy, if any, has not been quantified in these financial statements.

Under the Consolidated Omnibus Budget Reconciliation Act (COBRA), the Facility makes health care benefits available to eligible former employees and their eligible dependents. Certain requirements are outlined by the federal government for this coverage. The premium is paid entirely by the insured and there is no cost to the Facility under this plan.

## **10. FAIR VALUE OF FINANCIAL INSTRUMENTS**

FASB ASC 820-10 establishes a single authoritative definition of fair value, sets a framework for measuring fair value and requires additional disclosures about fair value measurements. Financial instruments that are measured and reported at fair value are classified and disclosed in one of the following categories based on inputs:

- Level 1 – Quoted market prices are available in active markets for identical instruments as of the reporting date.
- Level 2 – Pricing inputs are observable for the instruments, either directly or indirectly, as of the reporting date, but are other than quoted prices in active markets as in Level 1.
- Level 3 – Pricing inputs are unobservable for the instrument and include situations where there is little, if any, market activity for the instrument.

The following methods and assumptions were used by the Facility in estimating the fair value of its financial instruments:

Cash and assets whose use is limited – The carrying amounts reported in the balance sheet approximates fair value.

Accounts and other receivables – The carrying amounts reported in the balance sheet for accounts and other receivables approximates fair value because of the short-term nature of those instruments.

Estimated third-party payor settlements – The carrying amounts reported in the balance sheet for estimated third-party payor settlements approximates fair value because of the short-term nature of those instruments.

Accounts and other payables – The carrying amounts reported in the balance sheet for accounts and other payables approximates its fair value.

Long-term debt – The fair value of the is estimated using discounted cash flow analyses, based on the Facility's current incremental borrowing rates for similar types of borrowing arrangements.



## 10. FAIR VALUE OF FINANCIAL INSTRUMENTS (continued)

The carrying amounts and fair value of the Facility's financial instruments at June 30, 2013 and 2012 are as follows:

|  | June 30, 2013      |               | June 30, 2012      |               |
|--|--------------------|---------------|--------------------|---------------|
|  | Carrying<br>Amount | Fair<br>Value | Carrying<br>Amount | Fair<br>Value |
| Cash                                       | \$ 808,635         | \$ 808,635    | \$ 10,763          | \$ 10,763     |
| Assets whose use is limited                | 1,156,257          | 1,156,257     | 779,985            | 779,985       |
| Accounts and other receivables             | 1,901,283          | 1,901,283     | 1,683,826          | 1,683,826     |
| Estimated third-party payor<br>settlements | 57,655             | 57,655        | 701,676            | 701,676       |
| Accounts and other payables                | 1,423,440          | 1,423,440     | 1,660,155          | 1,660,155     |
| Long-term debt                             | —                  | —             | 767,512            | 767,512       |

## 11. EMPLOYEE HEALTH CLAIMS

Substantially all of the Facility's employees and their dependents are eligible to participate in the Facility's employee health, pharmacy and dental insurance plans. Beginning January 1, 2013, the Facility is self-insured for medical claims of participating employees and dependents up to per participant annual aggregate of \$25,000. Commercial stop-loss insurance coverage is purchased for health claims in excess of the aggregate annual amount. A provision is accrued for self-insured employee health claims including both claims reported and claims incurred but not yet reported. The accrual is estimated based on consideration of prior claims experience, recently settled claims, frequency of claims and other economic and social factors. It is reasonably possible that the Facility's estimate will change by a material amount in the near term.

Activity in the Facility's accrued employee health insurance and claims liability for the year ended June 30, 2013 is summarized as follows:

|  |                   |
|--|-------------------|
| Balance, beginning of year   | \$ —              |
| Current year claims incurred and changes in<br>estimates for claims incurred in prior years: |                   |
| Employer portion   | 918,809           |
| Employee portion   | 144,974           |
| Claims and expenses paid   | <u>(850,971)</u>  |
| Balance, end of year   | <u>\$ 212,812</u> |

## 12. CONTINGENCIES

In the normal course of business, the Facility is, from time to time, subject to allegations that may or do result in litigation. The Facility evaluates such allegations by conducting investigations to determine the validity of each potential claim. Based upon the advice of legal counsel, management records an estimate of the amount of ultimate expected loss, if any, for each case. Events could occur that would cause the estimate of ultimate loss to differ materially in the near term.

## **ADDITIONAL INFORMATION**

**KEARNY COUNTY HOSPITAL**  
**SCHEDULE OF PATIENT SERVICE REVENUE**

| Year ended June 30,              |              |               |               |              |               |               |
|----------------------------------|--------------|---------------|---------------|--------------|---------------|---------------|
| 2013                             |              |               | 2012          |              |               |               |
|                                  | Inpatient    | Outpatient    | Total         | Inpatient    | Outpatient    | Total         |
| Routine services:                |              |               |               |              |               |               |
| Acute                            | 1,039,955    | \$ -          | \$ 1,039,955  | \$ 864,290   | \$ -          | \$ 864,290    |
| Swing-bed                        | 994,104      | -             | 994,104       | 646,788      | -             | 646,788       |
| Nursery                          | 309,314      | 4,300         | 313,614       | 272,239      | -             | 272,239       |
| High Plains                      | 3,457,761    | -             | 3,457,761     | 3,263,774    | -             | 3,263,774     |
| Operating room                   | 409,611      | 609,372       | 1,018,983     | 271,238      | 514,511       | 785,749       |
| Labor and delivery               | 501,353      | 24,350        | 525,703       | 489,390      | 24,190        | 513,580       |
| Anesthesiology                   | 9,750        | 383,808       | 393,558       | 3,725        | 338,666       | 342,391       |
| Radiology                        | 230,444      | 1,466,486     | 1,696,930     | 136,169      | 1,325,469     | 1,461,638     |
| Laboratory                       | 727,776      | 3,080,933     | 3,808,709     | 541,796      | 2,593,294     | 3,135,090     |
| Respiratory therapy              | 148,482      | 32,791        | 181,273       | 160,644      | 28,752        | 189,396       |
| Physical therapy                 | 162,726      | 400,752       | 563,478       | 90,395       | 428,961       | 519,356       |
| Electrocardiology                | 9,940        | 63,925        | 73,865        | 15,185       | 58,294        | 73,479        |
| Medical supplies                 | 438,929      | 246,814       | 685,743       | 380,833      | 241,130       | 621,963       |
| Pharmacy                         | 886,675      | 485,735       | 1,372,410     | 821,107      | 441,185       | 1,262,292     |
| Heart monitors and cardiac rehab | 26,762       | 87,173        | 113,935       | 15,620       | 82,164        | 97,784        |
| Clinic                           | -            | 4,672,400     | 4,672,400     | -            | 4,048,904     | 4,048,904     |
| Emergency room                   | 20,901       | 952,609       | 973,510       | 20,402       | 921,449       | 941,851       |
| Observation care                 | 15,173       | 361,415       | 376,588       | 19,318       | 228,059       | 247,377       |
| Home health                      | -            | 145,334       | 145,334       | -            | 216,773       | 216,773       |
| Gross patient service revenue    | \$ 9,389,656 | \$ 13,018,197 | 22,407,853    | \$ 8,012,913 | \$ 11,491,801 | 19,504,714    |
| Less contractual adjustments     |              |               | (6,490,229)   |              |               | (4,980,409)   |
| Less charity care                |              |               | (127,463)     |              |               | (116,077)     |
| Less bad debts                   |              |               | (819,202)     |              |               | (725,144)     |
| Net patient service revenue      |              |               | \$ 14,970,959 |              |               | \$ 13,683,084 |

**KEARNY COUNTY HOSPITAL**

**SCHEDULE OF OPERATING EXPENSES BY FUNCTIONAL DIVISION**

| Department  | Year ended June 30, 2013 |                          |                     |                      | Percent<br>of total<br>operating<br>expenses |
|---|--------------------------|--------------------------|---------------------|----------------------|--|
|   | Salaries                 | Supplies<br>and<br>other | Depreciation        | Total                |  |
| Routine service:  |                          |                          |                     |                      |  |
| Adult and pediatrics  | \$ 987,568               | \$ 171,371               | \$ 109,004          | \$ 1,267,943         | 7.16 %                                       |
| Nursery   | 100,212                  | 8,231                    | 2,016               | 110,459              | 0.62   |
| High Plains (intermediate,<br>assisted living and<br>self-care) | 1,891,323                | 233,450                  | 361,811             | 2,486,584            | 14.01  |
|   | <u>2,979,103</u>         | <u>413,052</u>           | <u>472,831</u>      | <u>3,864,986</u>     | <u>21.79</u>                                 |
| Ancillary services:   |                          |                          |                     |                      |  |
| Operating room  | 238,364                  | 50,779                   | 44,990              | 334,133              | 1.88   |
| Labor and delivery  | 94,397                   | 19,025                   | 8,558               | 121,980              | 0.69   |
| Anesthesiology  | 217,596                  | 337,679                  | —                   | 555,275              | 3.13   |
| Radiology   | 211,844                  | 246,655                  | 63,969              | 522,468              | 2.94   |
| Laboratory  | 341,679                  | 336,654                  | 32,683              | 711,016              | 4.01   |
| Respiratory therapy   | 53,063                   | 7,210                    | —                   | 60,273               | 0.34   |
| Physical therapy  | 137,065                  | 6,339                    | 4,044               | 147,448              | 0.83   |
| Speech therapy  | —                        | 2,982                    | —                   | 2,982                | 0.02   |
| Electrocardiology   | 1,096                    | 258                      | —                   | 1,354                | 0.01   |
| Medical supplies  | 138,448                  | 128,273                  | —                   | 266,721              | 1.50   |
| Pharmacy  | 62,698                   | 180,886                  | 29,437              | 273,021              | 1.54   |
| Heart monitors and<br>cardiac rehab                             | 29,365                   | 9,925                    | 18,064              | 57,354               | 0.32   |
| Clinic  | 2,463,242                | 440,453                  | 56,321              | 2,960,016            | 16.68  |
| Emergency room  | 50,453                   | 120,928                  | 7,311               | 178,692              | 1.01   |
| Home health   | 150,170                  | 8,827                    | 875                 | 159,872              | 0.90   |
|   | <u>4,189,480</u>         | <u>1,896,873</u>         | <u>266,252</u>      | <u>6,352,605</u>     | <u>35.80</u>                                 |
| General services:   |                          |                          |                     |                      |  |
| Nursing administration  | 232,860                  | 16,303                   | 15,902              | 265,065              | 1.49   |
| Operation of plant  | 192,320                  | 627,801                  | 7,654               | 827,775              | 4.66   |
| Laundry   | 147,005                  | 74,455                   | 1,944               | 223,404              | 1.26   |
| Housekeeping  | 239,942                  | 42,151                   | —                   | 282,093              | 1.59   |
| Dietary   | 514,768                  | 330,126                  | 3,096               | 847,990              | 4.78   |
| Medical records   | 176,271                  | 78,620                   | 28,004              | 282,895              | 1.59   |
| Administration and general                                      | 687,185                  | 568,849                  | 25,271              | 1,281,305            | 7.22   |
| Employee benefits   | —                        | 2,965,963                | —                   | 2,965,963            | 16.71  |
| Depreciation - building   | —                        | —                        | 551,954             | 551,954              | 3.11   |
|   | <u>2,190,351</u>         | <u>4,704,268</u>         | <u>633,825</u>      | <u>7,528,444</u>     | <u>42.41</u>                                 |
|   | <u>\$ 9,358,934</u>      | <u>\$ 7,014,193</u>      | <u>\$ 1,372,908</u> | <u>\$ 17,746,035</u> | <u>100.00 %</u>                              |

| Year ended June 30, 2012  |                     |                          |                     |                      |  |
|---|---------------------|--------------------------|---------------------|----------------------|--|
| Department  | Salaries            | Supplies<br>and<br>other | Depreciation        | Total                | Percent<br>of total<br>operating<br>expenses |
| Routine service:  |                     |                          |                     |                      |  |
| Adult and pediatrics  | \$ 933,073          | \$ 86,026                | \$ 12,484           | \$ 1,031,583         | 6.11 %                                       |
| Nursery   | 94,709              | 8,887                    | 2,016               | 105,612              | 0.63   |
| High Plains (intermediate,<br>assisted living and<br>self-care) | 1,862,110           | 265,287                  | 390,876             | 2,518,273            | 14.93  |
|   | <u>2,889,892</u>    | <u>360,200</u>           | <u>405,376</u>      | <u>3,655,468</u>     | <u>21.67</u>                                 |
| Ancillary services:   |                     |                          |                     |                      |  |
| Operating room  | 201,729             | 52,345                   | 62,329              | 316,403              | 1.88   |
| Labor and delivery  | 101,806             | 18,055                   | 8,558               | 128,419              | 0.76   |
| Anesthesiology  | 241,846             | 292,515                  | —                   | 534,361              | 3.17   |
| Radiology   | 179,400             | 208,108                  | 103,043             | 490,551              | 2.91   |
| Laboratory  | 321,002             | 291,775                  | 18,296              | 631,073              | 3.74   |
| Respiratory therapy   | 47,552              | 14,561                   | —                   | 62,113               | 0.37   |
| Physical therapy  | 107,807             | 40,065                   | 1,647               | 149,519              | 0.89   |
| Speech therapy  | —                   | 1,575                    | —                   | 1,575                | 0.01   |
| Electrocardiology   | 1,006               | 620                      | —                   | 1,626                | 0.01   |
| Medical supplies  | 134,655             | 124,438                  | —                   | 259,093              | 1.54   |
| Pharmacy  | 58,080              | 195,596                  | 16,846              | 270,522              | 1.60   |
| Heart monitors and<br>cardiac rehab                             | 33,680              | 6,197                    | 18,064              | 57,941               | 0.34   |
| Clinic  | 2,247,508           | 381,997                  | 45,299              | 2,674,804            | 15.86  |
| Emergency room  | 40,674              | 173,763                  | 5,726               | 220,163              | 1.31   |
| Home health   | 173,143             | 26,517                   | 875                 | 200,535              | 1.19   |
|   | <u>3,889,888</u>    | <u>1,828,127</u>         | <u>280,683</u>      | <u>5,998,698</u>     | <u>35.58</u>                                 |
| General services:   |                     |                          |                     |                      |  |
| Nursing administration  | 265,129             | 38,520                   | 4,094               | 307,743              | 1.82   |
| Operation of plant  | 182,079             | 525,998                  | 5,958               | 714,035              | 4.23   |
| Laundry   | 130,068             | 71,799                   | 1,944               | 203,811              | 1.21   |
| Housekeeping  | 220,044             | 42,689                   | —                   | 262,733              | 1.56   |
| Dietary   | 475,681             | 243,360                  | 2,523               | 721,564              | 4.28   |
| Medical records   | 177,212             | 100,283                  | 28,004              | 305,499              | 1.81   |
| Administration and general                                      | 671,533             | 645,454                  | 12,572              | 1,329,559            | 7.88   |
| Employee benefits   | —                   | 2,772,223                | —                   | 2,772,223            | 16.44  |
| Depreciation - building   | —                   | —                        | 594,039             | 594,039              | 3.52   |
|   | <u>2,121,746</u>    | <u>4,440,326</u>         | <u>649,134</u>      | <u>7,211,206</u>     | <u>42.75</u>                                 |
|   | <u>\$ 8,901,526</u> | <u>\$ 6,628,653</u>      | <u>\$ 1,335,193</u> | <u>\$ 16,865,372</u> | <u>100.00 %</u>                              |